No. 512

In the Supreme Court of the United States

OCTOBER TERM, 1952

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v.

RALSTON PURINA COMPANY

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR SECURITIES AND EXCHANGE COMMISSION

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OPINIONS BELOW

The opinion of the Court of Appeals (R. 88-99) is reported at 200 F. 2d 85. The opinion of the District Court (R. 46-54) is reported in 102 F. Supp. 964.

JURISDICTION

The judgment of the Court of Appeals was entered on November 21, 1952 (R. 100). The jurisdiction of this Court is invoked under 28 U.S.C. 1254. See also Section 22(a) of the Securities Act of 1933 [15 U.S.C. 77v(a)].

QUESTION PRESENTED

Whether the exemption from registration provided in the Securities Act of 1933 for transactions "not involving any public offering" applies to an offering by a corporation to an indeterminate group of more than five hundred employees, including those who had no access to information concerning the issuer's affairs.

STATUTE INVOLVED

Pertinent provisions of the Securities Act of 1933, 48 Stat. 74, as amended, 48 Stat. 905, 15 U.S.C. 77a *et seq.*, are set forth in an appendix.

The question in this case involves the construction of the second clause of Section 4(1) of the Act [15 U.S.C. 77d(1)], which reads as follows:

> Sec. 4. The provisions of section 5 shall not apply to any of the following transactions:
> (1) * * * transactions by an issuer not involving any public offering; * * *

STATEMENT

This action was instituted by the Securities and Exchange Commission to enjoin Ralston Purina Company from selling its $25 par value common stock in violation of the registration requirements of Section 5(a) of the Securities Act of 1933 [15 U.S.C. 77e(a)] (R. 1-3). As the court of appeals pointed out, "The evidence in the instant case is virtually undisputed, although the Commission questions the validity of certain inferences drawn by the District Court" (R. 89-90).

Ralston Purina Company, a manufacturer and distributor of feed and cereals, has approximately 7,000 employees in its numerous mills, plants, warehouses, and stores scattered throughout the country.[1] It has been selling its common stock to many of its employees for a number of years. Since 1947 the actual sales, together with orders received in connection with the 1951 offering, which ceased on the institution of the present action, total almost two million dollars. It concedes that it has made use of the mails and facilities of interstate commerce in connection with these offerings (R. 4, 8).

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[1] In its answer the Company stated "that it has a nation-wide distribution of its products and that to facilitate such distribution operates a large number of mills, cereal plants, soybean processing plants, sanitation and farm supply distribution centers, warehouses, sales offices and stores all over the United States; that it has a large number of various departments and that the operation of its business is, so far as possible, decentralized so that the various operating units throughout the country have the responsibility for the conduct of their individual operation and that defendant has in the past five years very substantially increased the number and size of its plants of various types and the dollar volume of its business" (R. 4).

Its vice president testified (R. 57): "Ralston Purina operated 36 feed mills, 6 soybean processing plants, and 3 cereal mills. It also operates many warehouses and elevators, some of which are owned, but most of which are leased by the company. It operates 79 retail concerns and employs approximately 7,000 people."

Its major milling properties are at: "Amarillo, Tex., Battle Creek, Mich., Bloomington, Ill., Brawley, Calif., Buffalo, N. Y., Charlotte, N. C., Circleville, Ohio, Davenport, Iowa, Delmas, Del., Denver, Colo., Fort Worth, Tex., Iowa Falls, Iowa, Jackson, Miss., Kansas City, Mo., LaFayette, Ind., Los Angeles, Calif., Lubbock, Tex., Macon, Ga., Miami Fla., Minneapolis, Minn., Muskogee, Okla., Nashville, Tenn., Oakland, Calif., Oklahoma City, Okla., Omaha, Nebr., Pocatello, Idaho, Richmond, Ind., St. Johnsbury, Vt., St. Louis, Mo., Stockton, Calif., Tampa, Fla., Visalia, Calif., Wichita, Kans., Wilmington, Del." (R. 72).

The 1951 offering was authorized by the following resolution of Ralston Purina Company dated September 11, 1951 (R. 45):

> Resolved, that Mr. Donald Danforth, Mr. Lewis B. Stuart or Mr. E. R. Siler be and each of them is hereby *authorized to sell* at $80 a share, not to exceed 10,000 shares of the authorized but unissued common stock of Ralston Purina Company *to employees* of Ralston Purina Company or Ralston Purina Company of Canada, Ltd., *who shall,* without any solicitation by the Company, or its officers or employees, *inquire of any of them as to how to purchase common stock of Ralston Purina Company;* provided, however, that if such officer is able to purchase such stock for less on the open market he is authorized to purchase stock for such employee on the open market at such lesser price; provided further that this authorization shall terminate December 31, 1951. [Italics supplied.]

Similar resolutions had been used for the employee offerings of previous years (R. 64).

Pursuant to the resolution of September 11, 1951, the following memorandum was sent to the Company's branch and store managers (R. 59, 66):

> St. Louis, Missouri,
> September 21, 1951.
>
> If you would like to buy some Purina Common Stock at $80 a share, which is about the current market, let me know by October 1 how many shares you want.

The Company has issued the following statement which should be thoroughly understood by anyone interested in acquiring stock at this time.

"The Company is unwilling to take the responsibility, in essence, of guaranteeing or forecasting that the price of Purina stock is going up or will remain at its present price for the next twelve months or so. Consequently the Company is making no recommendation that employees purchase at current prices.

"The Company, however, is willing to try to protect employees against a market rise in the price of the stock resulting from temporary competitive bidding by employees. To do this the Company will make available for a limited time some authorized but unissued stock at $80.00 a share. *The only employees to whom this stock will be available will be those who take the initiative and are interested in buying stock at present market prices.*

"If stock can be purchased on the open market at a price lower than $80 a share, the employee will, of course, buy at the lower price."

H. A. STEIN.

* * * * *

[Italics supplied.]

The actual number of employees to whom the Company's offerings have been made is not known since the Company kept no record of these offerees, but the offerees each year have admittedly exceeded the actual purchasers (R. 8-9). One hundred sixty-seven employees accepted the 1951 stock

offering before it was withdrawn pending resolution of the issue here involved (R. 39). These acceptances involved 3,769 shares at $301,520 (R. 39). The offer was made to a substantially larger number. According to the Company's witness, its vice president, Mr. Stuart, the offering was to more than 500 but less than 1,000.[2] In 1947 the Company received $331,740 by the sale of 6,984 shares to 243 employees at $47.50 per share (R. 11). In 1948 it received $56,000 by the sale of 1,120 shares to 20 employees at $50 per share (R. 18). In 1949 it received $550,000 by the sale of 10,000 shares to 414 employees at $55 per share (R. 19). In 1950 it received $676,130 by the sale of 9,659 shares to 411 employees at $70 per share (R. 29). These sums total almost $2,000,000.

Although the sole limitation expressed in the corporate resolution and the memorandum sent to store managers was that the offering was to be made only to employees who evidenced a desire to buy the stock, the Company has contended that the offer was open only to "key employees". This term was defined differently at different times.

In response to an inquiry by this Commission, Mr. Stuart had stated (R. 82):

> Criterion employed to determine if a person is a key employee is position held, namely, an officer, department head, assistant to a de-

[2] Although Mr. Stuart had advised the Commission that the number of employees eligible to purchase stock was "approximately five hundred" (R. 82), when cross-examined in this connection he testified: "It was not certainly exactly 500, but it was not a thousand, but let us say, or any number substantially above that" (R. 62).

partment head or other employee the company considers eligible for promotion to a position of greater responsibility as an administrative, production, sales, or research department head or an assistant to a department head.

The "position held" by employees who have actually purchased stock from the Company during the past few years, however, has included:

Artist (R. 18).
Assistant in Animal Pathological Dept. (R. 13).
Assistant District Salesman (R. 20).
Assistant Grain Buyer (R. 21).
Assistant Purchasing Agent (R. 11).
Assistant Superintendent (R. 34).
Bakeshop Foreman (R. 22).
Buyer (R. 15).
Cashier (R. 12).
Chemist (R. 41).
Chow Loading Foreman (R. 34).
Clerical Assistant to Accounting Manager (R. 20).
Clerical Assistant in Cashier Department (R. 20).
Copywriter (R. 19).
Dairy Specialist (R. 42).
District Salesman (R. 16).
Dog Chow Specialist (R. 37).
Electrician—Maintenance Dept. (R. 20).
Elevator Foreman (R. 15).
Engineer (R. 34).
General Night Foreman (R. 34).
Intermediate Grain Merchandiser (R. 19).
Laboratory Assistant (R. 21).
Loading Foreman (R. 22).

Mail Section Supervisor (R. 20).
Maintenance Shift Leader (R. 21).
Manager of Eastport Warehouse (R. 32).
Mill Office Clerk (R. 40).
Mill Production Trainee (R. 32).
Miller (R. 21).
Millwright Foreman (R. 21).
Night Foreman (R. 32).
Office Production Assistant (R. 31).
Order-Credit Trainee (R. 40).
Power Engineer (R. 15).
Production Trainee (R. 21).
Ralston Miller (R. 34).
Retail Salesman (R. 12).
Secretary to Production Manager (R. 13).
Shipping Clerk (R. 21).
Stenographer to Staff Manager (R. 15).
Stock Clerk (R. 23).
Territory Salesman (R. 17).
Tinsmith Foreman (R. 32).
Traffic Clerk (R. 21).
Veterinarian (R. 41).

Among the purchasers of stock from the Company were employees whose total annual compensation was as low as $2,700 (in 1949), $2,435 (in 1950), and $3,107 (in 1951) (R. 46). The employees who purchased the Company's stock, many of whom were from rural areas (R. 58), were scattered across the United States.[3]

[3] Purchasers resided in the following communities:

Atlanta, Georgia (R. 12).
Austin, Texas (R. 28).
Baltimore, Maryland (R. 17).
Battle Creek, Michigan (R. 15).
Binghamton, New York (R. 25).
Bloomington, Illinois (R. 21).
Boston, Massachusetts (R. 12).

After the classification and salary ranges of the employees who had purchased stock from the Company had become a matter of record in these proceedings, Mr. Stuart expanded his definition of a "key employee" (R. 58):

> A key employee of course can be an officer or a department head or an assistant to a department head but is not confined to an organization chart. It would include an individual who is eligible for promotion, an individual who especially influences others or who advises others, a person whom the employees look to in some special way, an individual, of

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Buffalo, New York (R. 11).
Charlotte, North Carolina (R. 14).
Chicago, Illinois (R. 12).
Chattanooga, Tennessee (R. 36).
Circleville, Ohio (R. 14).
Cleveland, Ohio (R. 12).
Columbus, Ohio (R. 17).
Davenport, Iowa (R. 15).
Delmar, Delaware (R. 39).
Denver, Colorado (R. 15).
Des Moines, Iowa (R. 16).
Detroit, Michigan (R. 20).
Dundee, Michigan (R. 22).
Fort Worth, Texas (R. 12).
Garland, Texas (R. 37).
Gray Summit, Missouri (R. 13).
Iowa Falls, Iowa (R. 14).
Jackson, Mississippi (R. 39).
Jacksonville, Florida (R. 16).
LaFayette, Indiana (R. 22).
Los Angeles, California (R. 15).
Lubbock, Texas (R. 14).
Memphis, Tennessee (R. 12).
Miami, Florida (R. 22).
Minneapolis, Minnesota (R. 14).
Nashua, New Hampshire (R. 41).
Nashville, Tennessee (R. 14).
New York, New York (R. 12).
Newark, Delaware (R. 42).
Oakland, California (R. 15).
Omaha, Nebraska (R. 14).
Pocatello, Idaho (R. 15).
Philadelphia, Pennsylvania (R. 12).
St. Johnsbury, Vermont (R. 23).
St. Louis, Missouri (R. 11).
San Francisco, California (R. 12).
Seattle, Washington (R. 12).
Stockton, California (R. 23).
Syracuse, New York (R. 12).
Tampa, Florida (R. 23).
Toronto, Ontario (R. 25).
Visalia, California (R. 15).
Wichita, Kansas (R. 23).
Wilmington, Delaware (R. 15).

> course, who carries some special responsibility, who is sympathetic to management and who is ambitious and who the management feels is likely to be promoted to a greater responsibility.

Subsequently, Mr. Stuart appeared to equate "key employees" to "sales people"[4] and to "production people" (R. 60). He claimed, however, that they did not include "little people in our organization" (R. 60).

In an attempt to clarify his testimony, Mr. Stuart stated on cross-examination (R. 61):

> Well, sir, I think that is a matter of influence. I think all of us who have handled people know that there are key people in the various echelons if you have been in military service there were a captain, who perhaps would have felt that one of the lieutenants was a key lieutenant, but you know if you did not have the support of your key sergeant, or the key corporal, or maybe the key private who exercised influence, that you better not go into anything that is very serious; and the same is true in business. Key people are simply not regimented into charts. We don't regiment people in that manner.

Mr. Stuart's own testimony confirmed what the resolution and offering letter show on their face, that the term "key employee" appears to have in-

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[4] Of the total number of purchasers and would-be purchasers, approximately one-third were salesmen (R. 11-44).

cluded any employee who might have "indicated an interest" in the purchase of the stock (R. 59).[5]

Some information concerning the financial affairs of the Company had been sent to those of the offerees who were already stockholders (R. 67-72), but a substantial portion of the offerees were not stockholders (R. 11-44). Mr. Stuart, testified that figures available to him as an officer "were not available to all of the so-called key employees".[6] The Company's production records were apparently available to many of its employees to whom its stock was offered (R. 60, 63), but it is not contended that the numerous items of information which would have been required in a prospectus

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[5] Mr. Stuart testified that when stock was available to employees, the procedure was as follows: "The president, speaking for the board of directors, notified the officers, who in turn notified the managers working directly under them, that the company had or was about to make some stock available. They [the managers] very carefully were told not to solicit in any way orders for stock, but simply to acquaint the people who had indicated an interest or whom they felt it was fair to notify of the situation" (R. 58-59).

Although Mr. Stuart stated that there were many employees who had been turned down when asking to purchase stock (R. 61), he cited no substantiating details, and it appears from the Company's brief in the court below (p. 15), that he was referring not to the offerings by the Company, which were apparently made only in September or October of each year, but to purchases for employees on the open market, an accommodation which Mr. Stuart sometimes performed.

[6] This testimony appears at R. 66:

> Mr. Stuart stated that depending on the individual all figures are available to some, and to a lesser degree to others. He also stated that he was vice president of the company and that figures were available to him showing the profits of Ralston Purina for a given month. He stated that these figures were available to many others but that they were not available to all of the so-called key employees.

if the stock had been registered were generally available to them. These would include any change in the trend of profits in the period subsequent to the last published financial statements. Although Mr. Stuart emphasized that "tonnage, this is volume production, is perhaps the biggest single figure in the company's success," it does not necessarily follow that the ratio between production and profits is constant. For example, according to the Wall Street Journal of December 15, 1951 (R. 63, 82):

> Despite a 35% jump in sales, net income of Ralston Purina Co. for the fiscal year ended September 30 fell to $8,784,341, from the $12,560,665 reported for the preceding year * * *.[7]

It was in September 1951, before these figures were generally available, that the offering which was stopped by the present litigation was being made to employees (R. 63, 66).

The Company states that the purpose of its sales to "key employees" was to enable employees who received a bonus to acquire common stock of the Company without bidding up the price of the stock, which was dealt in only on the over-the-counter market and in limited quantities (R. 5-6). The Company, however, has at no time made the claim that its stock was offered *only* to employees who re-

[7] The 1951 earnings were charged approximately $500,000 to reflect excess profit taxes for the 1950 fiscal year of which the company was not aware "when we closed our books at the end of 1950" (R. 83, 63). If the published figures were adjusted retroactively to make this charge in 1950, they would show $9,284,794 for 1951 and $12,060,212 for 1950. Compare the company's report dated December 14, 1951 which confirms the 35 per cent increase in sales, while disclosing a 20 per cent drop in net profit after taxes (R. 67).

ceived a bonus. Nor has there been any constant relationship between the size of the bonuses and the amount of stock purchased by employees.[8]

Prior to the Company's 1950 offering, the Commission's Division of Corporation Finance advised it that in the Division's opinion the Company's apparent reliance on the Section 4(1) exemption in a previous offering "was not well founded" and suggested the advisability of communicating with the Commission "prior to making any future offering of securities" (R. 77). Without advising the Commission, however, in September 1950, the Company made the offering to its employees which resulted in the purchase of 9,659 shares by 411 employees that month (R. 29). After this fact became known to the Commission, in August 1951 it initiated the exchange of correspondence which led to the present action for an injunction (R. 76-77, 78-82).

Upon the institution of this action, the Company consented to a preliminary injunction. After hearing, the district court denied a permanent injunction decree on the ground that the sales were within the exemption from registration provided in Section 4(1) of the Act for "transactions by an issuer not involving any public offering." The court below affirmed, stating that it would not reverse the judgment of the trial court (R. 99) unless

[8] In this connection, for example, in 1947, when a bonus of $782,000 was distributed to 256 employees, 243 employees purchased $331,740 of stock from the Company, while in 1948, when a bonus of $734,000 was given to 252 employees, only 20 employees purchased stock from the Company and in the amount of only $56,000 (R. 11, 18, 59).

it could "demonstrate, at least to its own satisfaction, that the judgment is wrong," and that it was unable to do so in this case. By stipulation the Company agreed not to make further offerings to employees pending disposition of the matter in the appellate courts (R. 55-56, 100-101).

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals erred:

1. In finding that the Respondent's offering to its employees was not a public offering under Section 4(1) of the Securities Act; and

2. In upholding the District Court's order dismissing the complaint.

SUMMARY OF ARGUMENT

The interpretation of the private offering exemption by the court below conflicts with the purpose of the Securities Act to provide full and fair disclosure concerning security offerings. Both the text of the exemption and its context show that Congress did not intend to withhold the protection of registration from any substantial number of the public, but only in the case of isolated transactions with an individual or a small group. The "public" intended to be protected includes large groups of employees—clerks, salesmen, foremen, trainees, etc.—who participated in the offerings in question. Where an offer is not confined to those whose special circumstances make the protection of registration unnecessary it does affect the "public" and cannot qualify for exemption under the test "not involving any public offering."

In the instant case, the company failed to prove that its offering was not made to substantially all of its 7,000 employees; but even if the record supported the contention that the offering was limited to about 500 employees, as contended, the number of offerees would still preclude application of the exemption here involved, particularly since the criteria allegedly used to select the group were unrelated to the purpose of the Act. These include the motive of the issuer to create employee goodwill and the absence of high pressure sales techniques. Only confusion can result from determining the application of the exemption upon the basis of irrelevant criteria of this nature.

The decision below is inconsistent with the previously decided cases and the legislative history, which indicate that the exemption here involved is "to permit an issuer to make a specific or isolated sale of its securities." The legislative background of the Act, as passed in 1933, is not altered by certain contradictory explanations for the rejection in 1934 of an amendment which would have exempted offerings to employees.

The exemptions, which are specifically applicable to exchanges with existing security holders, would be surplusage and the limitations thereon nugatory, if, as indicated by the court below, the private offering exemption applies to offerings to a substantial group of offerees wherever there is a "logical basis" for giving special consideration to the particular group.

Respondents' arguments to the effect that the stock offering issue is relatively small and the burden of registration relatively heavy do not establish the availability of the non-public offering exemption. Congress has dealt specifically with the problem of small issues, and has made the availability of an exemption on that basis depend upon conditions not applicable in this case.

Weight should be given to the consistent construction of the exemption by the Commission, a construction well established and judicially accepted prior to a 1945 amendment which liberalized the small issue exemption, but did not undertake to change the non-public-offering exemption.

ARGUMENT

Although the term "public offering" is not defined, both the pattern of the Act and its legislative history make clear that the unregistered offering which the Commission seeks to enjoin is not exempt. This result is in accord with the decided cases, except for the decisions below, and conforms to the consistent administrative interpretation.

This Court has pointed out that the Securities Act must be construed "in conformity with its dominating general purpose . . . so as to carry out in particular cases the generally expressed legislative policy."[9] The "essential purpose of the statute is to protect investors by requiring publication of certain information concerning securities before

[9] *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U.S. 344, 350-351.

offered for sale."[10] The title of the Act itself describes it as "An Act to provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails . . ."

Section 5, requiring registration and the use of a statutory prospectus, is the heart of the Act; and the exemption provisions of Section 3 and 4 serve primarily to determine whether or not Section 5 is applicable.[11] Subsidiary provisions deal with the mechanics of registration (Section 6), information required in a registration statement (Section 7), the procedure for the taking effect of registration statements and amendments (Section 8), the information required in a prospectus (Section 10), and civil liabilities on account of a false registration statement or a sale in violation of Section 5 (Sections 11 and 12(1)). In addition there are general procedural and enforcement provisions, criminal sanctions and provisions for judicial review.

This case turns on Section 4(1), which exempts from Section 5 "transactions by an issuer not involving any public offering." In holding the instant $800,000 offering to come within this exemption, the court below stated (R. 93):

> The Company had the burden of proving that its offering of stock to its key employees

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[10] *A. C. Frost* v. *Coeur d'Alene Mines Corp.*, 312 U.S. 38, 40.

[11] The Act also contains broad anti-fraud provisions applicable to any sale of a security which involves the use of interstate instrumentalities or the mails, including sales exempt from Section 5. See Section 17 and 12(2).

> came within the exemption provided by Section 4(1) of the Act, which, being an exception to the general policy of the Act, is to be strictly construed and may not receive such a broad construction as would be destructive of the plain purpose which caused the Act to be adopted.

The Court also appeared to recognize that an offer is made to all to whom the stock is "made available" (R. 92).

It rejected, however, any thought that the exemption was intended to apply only "to specific or isolated sales or offerings of securities by an issuer to a particular person or to a numerically small group" (R. 95-96), and disagreed with the contention that the offerings in the instant case "were made to too many employees and involved too many shares of stock to be nonpublic offerings" (R. 97). It concluded (R. 98):

> * * * we do not think that the intra-organizational offerings of stock by the Company, unaccompanied by any solicitation, which have resulted in a limited distribution of stock, for investment purposes, to a select group of employees considered by the management to be worthy of retention and probable future promotion, is to be excluded from the exemption of nonpublic offerings granted by Congress. There is, we think, virtually no possibility that these offerings, if continued, will frustrate or impair the purpose of the Act.

The construction of the exemption by the court below does materially impair the purpose of the Act by sanctioning the withholding of the prescribed disclosures from a substantial number of offerees who have not been shown to be without need for its protections and in an area where the Act did not contemplate that the burden of registration might be disproportionate to the contemplated benefits. Instead of actually construing the exemption strictly, the opinion below subtly shifts to the Commission the burden of showing that exemption should be denied.

a. *The text of Section 4(1) supports a construction that an offering to a substantial number of the public is not exempt.*

The text, "not involving any public offering," while not employing words of art, derives "much meaningful content from the purpose of the Act, its factual background and the statutory context." *Cf. American Power and Light Co. v. Securities and Exchange Commission*, 329 U. S. 90, 104.[12] On

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[12] For a discussion of prior English interpretation of § 81 of the English Companies Act applicable to "any prospectus, notice, circular, advertisement, or other invitation, offering to the public," see Douglas & Bates, Some Effects of the Securities Act upon Investment Banking, 1 Univ. of Chicago L. Rev. 283, at p. 299.

See *Nash* v. *Lynde*, [1929] A. C. 158, discussed in 167 L. T. 239 (1929), where Viscount Sumner said:

> The public * * * is of course a general word. No particular numbers are prescribed. Anything from two to infinity may serve; perhaps even one, if he is intended

its face the exemption is inapplicable if there is involved "any public offering". This does not mean that all members of the public must be included. As the opinion below concedes, Congress could not have "intended that an offering not open to everyone was exempt" (R. 94). On the other hand one of the situations where the exemption does apply is an offering to a few institutional investors who make their own investigation and who are in a position to negotiate the details of the transaction with the issuer.

The Commission has construed the exemption with major emphasis on whether the offering is calculated to reach a substantial number of "the public" sought to be protected.[13] The Commission has rarely acquiesced in a claim for exemption where as many as a hundred offerees have been in-

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to be the first of a series of subscribers but makes further proceedings needless by himself subscribing the whole.

and Lord Buckmaster added:

> A distribution of a prospectus among a well-defined class of the public would be an issue within the meaning of Section 81.

[13] The President's message initiating the federal securities legislation expressed concern for "the public" which had "sustained severe losses" and stated:

> The purpose of the legislation I suggest is to protect the public with the least possible interference to honest business.
>
> This is but one step in our broad purpose of protecting investors and depositors. [77 Cong. Rec. (1933) 937].

Similarly, the Senate Report speaks of the bill as one "to protect the investing public" and based on the policy "of informing the investor." S. Rep. No. 47, 73d Cong., 1st Sess. (1933) 1. It seems clear from the foregoing statements that the "public" sought to be protected included any investors who might be expected to need the protection of the Act.

volved and then only in circumstances where for special reasons the protections of the act appear not to be necessary.[14] Such might be the case where an offering is made to the top management of the issuer who can be expected to be familiar with the type of information that would be available by a statutory prospects. But, whatever the special circumstances, the Commission has consistently interpreted the exemption as being inapplicable when a large number of offerees is involved.

Such an interpretation is necessary if the exemption is to be construed so as not to impair the disclosure purposes of the Act. This approach conforms to what was stated to be the purpose of the exemption provisions of the Act taken as a whole. The Committee on Interstate and Foreign Commerce said in discussing the scope of the bill as reported to the House:

> It carefully exempts from its application certain types of securities and securities transactions where there is no practical need for its application or where the public benefits are too remote.[15]

Since the offerings here in question went to hundreds of employees throughout the country,

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[14] A 1934 published opinion of the Commission's then General Counsel, set forth in the opinion below (R. 96, n. 2), indicated that an offering designed to reach less than 25 ultimate purchasers would normally be regarded as within the exemption.

[15] H. Rep. No. 85, 73d Cong., 1st Sess. (1933) 5.

with most of those accepting purchasing in lots of less than a hundred shares, and many in amounts from one to ten shares,[16] it can hardly be contended that the offering did not extend to a substantial number of the public. Even if reference were made only to those employees who actually purchased or subscribed for petitioner's stock, the size of the group, in excess of 400 in each of two recent years, was so great that the exemption was not available.

The record makes clear, however, that the offering was to a much larger group. As noted by this Court, "the Securities Act prohibits the offer as well as the sale of unregistered, non-exempt securities." [17] Since the company had the burden of establishing the availability of the exemption, as the Court below concedes, it had the burden of showing that the offer rather than the sale was confined within the scope of the exemption. It failed, however, to keep any record of the number of its employees who were specifically invited to subscribe. With respect to the offerings in 1947, 1948, 1949, and 1950, there is absolutely nothing in the record to indicate the number of employee offerees except the company's concession that they exceeded the number of purchasers (R. 8-9). With respect to the 1951 offering the company conceded that it was made to "between 400 and 500 employees" (R. 8, 82), but on cross-examination the company's vice

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[16] See R. 11-45 listing the names and amounts of the several subscriptions.

[17] *Securities and Exchange Commission* v. *W. J. Howey Co.*, 328 U. S. 293, 301.

president was unable to give any rational explanation as to how these figures were arrived at (R. 61-62) and the Court below stated that it seemed "probable that the estimate of the Company was low" (R. 92). As we have seen, no limitation was set forth in the director's resolution authorizing the offering, and all branches and stores were concededly advised of the availability of the offering to employees by a letter indicating that the only limitation was that the employee "take the initiative" and be "interested in buying stock at present market prices." (See pp. 4-5, *supra.*) Accordingly, it would appear that the offering actually extended in the statutory sense to all of the 7,000 employees. To the extent that the courts below appear to have found a less extensive offering their findings appear to us to reflect an unduly restricted concept as to what constitutes an "offering".

Securities and Exchange Commission v. *Sunbeam Gold Mines Company*, 95 F. 2d 699 (C.A. 9) held an offering for cash to existing security holders, some 530 in number to be public and not exempt from registration. The security holders in question were the stockholders in one or another of two corporations which were to be merged; but the opinion indicates that the result would have been the same if only a single corporation had been involved. The court concluded at p. 702:

> We therefore hold that an offering of securities under the Securities Act of 1933 may be a public offering though confined to stock-

holders of an offering company, *a fortiori* where the offerees include the stockholders of another company, though seeking to become stockholders of the offeror.

This case is in point here. The number of offerees involved was at least as small as the offerees here and the limitation to persons who were stockholders of the corporations involved in the merger likewise involved logical motives on the part of the issuer in selecting the particular group. Neither employees as a class nor stockholders as a class are likely to be fully informed as to the issuer's affairs, although many members of either class would have more information than other members of the public.

The *Sunbeam* decision has been cited with approval in the following cases: *Merger Mines Corporation* v. *Grismer,* 137 F. 2d 335, 341 (C.A. 9, 1943), where an offering to 1,100 stockholders was found to be a public offering; *Kaufman* v. *United States,* 163 F. 2d 404, 410 (C. A. 6, 1947), where the trial court's charge to the jury on "public offering" was sustained on the basis of the *Sunbeam* decision; *Corporation Trust Co.* v. *Logan,* 52 F. Supp. 999, 1002 (D. Del. 1943), where the court cited with approval the language from the *Sunbeam* case that "an offering to stockholders, other than a very small number [is] a public offering ***"); *Campbell* v. *Degenther,* 97 F. Supp. 975, 977 (W.D. Pa. 1951), where the court cited the *Sunbeam* case for the proposition that "an offering of securities under the Securities Act of 1933 may be a public offering even though confined to stockholders of an offer-

ing company." *Securities and Exchange Commission* v. *Searchlight Consolidated Mining & Milling Co.* (D. Nev., No. 1000, March 17, 1953), where the Commission's motion for summary judgment was granted on the basis of the *Sunbeam* case in an action to enjoin Section 5 violations, despite a contention (which the Commission disputed but which the Court apparently found unnecessary to resolve) that the solicitation was confined to the defendant corporation's stockholders, approximately 400 in number.[18] A similar approach is reflected in decisions under State blue sky laws. See e.g., *People* v. *Montague*, 280 Mich. 610; 274 NW. 347, 350.

b. *The legislative history supports the Commission's construction.*

In reaching the conclusion that the offering involved in the *Sunbeam* case was exempt, the Ninth

[18] *Cf.*, however, *Securities and Exchange Commission* v. *Federal Compress & Warehouse Co.*, CCH Fed. Sec. Law Serv., 1941-1944 Dec., p. 90,117 (W.D. Tenn. 1936), a case relied upon below by the respondent. That case was decided prior to the *Sunbeam Gold Mines* case. There a preliminary injunction which would have stopped the sale of unregistered stock to the defendant's existing stockholders was denied. But in that case the court was concerned with the possibility that "the defendant corporation and its stockholders could and probably would be irreparably injured without any opportunity for redress" by issuance of the temporary injunction prior to the hearing on the merits (p. 90,122). The court also found that the stock there involved was "rather closely held in Memphis and environs," and that all of the stockholders had "full opportunity to become familiar with the affairs and conditions of the company through their contacts with . . . [its] officers and directors, statements sent to them from time to time and otherwise" (p. 90,118). Prior to any hearing on the merits and subsequent to an unsuccessful attempt on the part of the Commission for a temporary injunction *pendente lite* from a judge of the Court of Appeals for the Sixth Circuit, the action was dismissed on the ground that it had become moot.

Circuit relied in part upon the principle that the exemption, as an exception to the general policy of the legislation, must be narrowly confined, and relied in part upon the legislative history. This legislative history included a statement of the House Committee on Interstate and Foreign Commerce with respect to an earlier form of this exemption not differing materially from the present language,[19] that the purpose of the exemption is

> * * * to permit an issuer to make a specific or an isolated sale of its securities to a particular person, * * * [H. Rep. No. 85, 73d Cong., 1st Sess. (1933) p. 15-16].

The bill as it passed the House had exempted the sale of stock to existing stockholders. The Senate's elimination of this exemption was approved in conference and the following explanation given by the managers on the part of the House: "Sales of stock to stockholders become subject to the act unless the stockholders are so small in number that the sale to them does not constitute a public offering." See H. Rep. No. 152, 73d Cong., 1st Sess., (1933) p. 25. Rejection of the exemption provided in the House bill shows that there was no intention to exempt sales to groups having some special relationship to the issuer unless they should be "small in number".

The Securities Act was amended in 1934. One proposed exemption, which was rejected, would

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[19] The House draft, to which this statement referred, exempted "transactions by an issuer not with or through an underwriter and not involving any public offering." H.R. 5480 (May 4, 1933 draft) 73d Cong., 1st Sess., Sec. 4(1).

have exempted participants in employees' stock investment plans. The reasons of the House conferees for rejecting this amendment are clear and unambiguous, as stated in their report of the conference:

> The conferees eliminated the third proposed amendment to this subsection on the ground that the participants in employees' stock-investment plans may be in as great need of the protection afforded by availability of information concerning the issuer for which they work as are most other members of the public. [H. Rep. No. 1838, 73d Cong., 2d Sess., p. 41.]

The debate in the Senate, however, leaves some uncertainty as to the reasons of the Senate for not pressing the amendment. Senator Hastings, who had offered the rejected amendment, complained of its abandonment by the Senate conferees, stating: "I do not see why the Federal Government should insist upon having anything to do with a plan of a corporation which decides that, as a part of its policy, it will give certain additional compensation or bonus to its employees." Senator Couzens, one of the conferees, stated that "one of the controlling factors which caused the elimination of the amendment was the Insull transactions," and that "the House conferees were very insistent upon pointing out the evils which have occurred where employees of a number of corporations have been induced to buy shares of the stock of the corporations." (78 Cong. Rec. (1934) 10181) Senator

Fletcher, another conferee, suggested that the proposed amendment had been rejected as unnecessary because in the judgment of the conference no public offering would be involved, "and certainly there is no question in the world that the Commission has the authority to declare that such an offering would not be a public one." (78 Cong. Rec. 10182.)

The opinions below refer to Senator Fletcher's remarks, not to those of Senator Couzens, and conclude, erroneously we believe, that the legislative history offers no positive support for the Commission's construction (R. 50, 95). The Committee Report is entitled to more weight than the remarks of individual conferees in debate on the Senate floor, particularly when the Senators disagree. The fact of the rejection of the amendment exempting all employees' stock investment plans also warrants an inference that Congress did not mean to incorporate such an exemption in the Act, although we do not lean too heavily on the rejection of the amendment as positive support for the Commission's position. Certainly the court below could not properly draw the contrary conclusion from the proposed amendment's history. This episode is not part of the legislative history of the Securities Act as enacted, and is not in itself, of course, ground for supplying by judicial construction an amendment which the Congress itself rejected.

c. The specific exemption of exchanges with existing security holders indicates an intent not to include in the private offering exemption offerings to groups identified by special relationship to the issuer.

In rejecting the contention that an offering to a substantial number of offerees is necessarily "public," the courts below placed great reliance upon the issuer's designation of the offerees in question as "key employees." This was regarded not as a means of confining the offering to those top executives who would have no real need for the information which a registration statement would supply, but as showing that in its selection the respondent was prompted by legitimate business motives and not merely by a desire to avoid registration. These motives were described by the district court as related to forging ties of loyalty between itself and its employees (R. 52), and lacking "the slightest suggestion of a device to evade the law . . ." (R. 54). The Court of Appeals in turn characterized the selection as not "random or by lot or without any logical basis" (R. 99). In addition, it was noted that a substantial percentage of the offerees were already stockholders of the company and that as stockholders or as employees they might be assumed to have some knowledge of its affairs (R. 92). There was no finding, however, that all of the offerees, or even a substantial percentage of them, had access to information at all comparable to that

which would be afforded by registration.[20] Surely, the clerical employees, salesmen, foremen, trainees, etc., who purchased the Company's securities could not be expected to have had familiarity with the type of information required to be supplied by a statutory prospectus.

Apart from difficulties in stretching the language of the exemption in question to cover so broad an offering, this aspect of the decisions below appears inconsistent with the explicit consideration which the Act shows was given by Congress to offerings to existing stockholders. Sections 3(a)(9) and (10) provide exemptions for certain offerings to existing stockholders which might be wholly unnecessary if the court below should be upheld in its interpretation of the non-public offering exemption.[21] There is frequently a "logical basis for the

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[20] It has not been contended that the company's annual reports, as filed with the Commission or as distributed to stockholders, contained disclosures comparable to those which would have been required if the issue were registered. The sales and production records available to offerees in their capacity as employees were shown by the record to be a deceptive measure of profits. At the time the injunction action was brought the company's sales figures showed a substantial increase for the fiscal year which was ending; while the net profits for the year actually fell off sharply as a result of an increased tax item (p. 12, *supra*).

[21] Section 3(a)(9) exempts:

> Any security exchanged by the issuer with its existing security holders exclusively where no commission or other remuneration is paid or given directly or indirectly for soliciting such exchange;

Section 3(a)(10) exempts:

> Any security which is issued in exchange for one or more bona fide outstanding securities, claims or property interests, or partly in such exchange and partly for cash, where the terms and conditions of such issuance and ex-

selection" in confining an offering to existing security holders, particularly where preemptive rights are applicable or in the case of a reorganization, as well as a basis for assuming some prior knowledge of the issuer's affairs on the part of the offerees. In the case of such an offering it may frequently be urged, at least as validly as in the instant case, that the issuer's motive is primarily to accord the offerees an investment opportunity rather than to drive the sharpest possible bargain with them. Nevertheless these exemptions specifically applicable to offerings to existing stockholders are applicable only in the case of exchange transactions. In the non-reorganization situations covered by Section 3(a)(9) the exemption is applicable only where the new security is exchanged "exclusively"—i.e., no cash payment is involved [22]—and only where "no commission or other remuneration is paid or given directly or indirectly for soliciting such exchange." The reorganization exemption provided by Section 3(a)(10) applies only where the exchange is pursuant to a plan, the fairness of which has been approved by a court or agency authorized by law to grant such approval.

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change are approved, after a hearing upon the fairness of such terms and conditions at which all persons to whom it is proposed to issue securities in such exchange shall have the right to appear, by any court, or by any official or agency of the United States, or by any State or Territorial banking or insurance commission or other governmental authority expressly authorized by law to grant such approval."

[22] See Loss, *Securities Regulation* (1951) 363.

As we note *supra* (p. 26), the bill as it passed the House had contained a broader exemption which covered "the issuance of additional capital stock of a corporation sold or distributed by it among its own stockholders exclusively, where no commission or other remuneration is paid or given directly or indirectly in connection with the sale or distribution of such increased capital stock."[23] The conferees in substituting the present Section 3 (a) (9), limited to exchange transactions, stated: "Sales of stock to stockholders become subject to the act unless the stockholders are so small in number that the sale to them does not constitute a public offering." H. Rep. No. 152, 73d Cong., 1st Sess., at p. 25. To the extent that the exemption afforded in Section 3(a) (9) depends on the absence of sales commissions paid directly or indirectly, there is some analogy to what the court below characterized here as "unaccompanied by any solicitation" (R. 98). But it is inconsistent both with the text of Section 3(a)(9) and the changes in conference to conclude that Congress intended the absence of selling commissions to be a basis for exemption, except in the limited area to which Section 3(a) (9) extends.

d. *Congress made specific provision for an exemption of small offerings upon conditions not applicable here.*

In the court below respondent emphasized the alleged burdens of compliance with the registra-

[23] See H.R. 5480, Rep. No. 85, 73d Cong., 1st Sess., print of May 10, 1933 (showing Senate amendments), Sec. 4(3), at p. 9.

tion requirements of the Act, and indicated that these burdens were disproportionate to the potential benefit to those affected by the instant offering. The opinion below quotes the testimony of an officer of the respondent as to the alleged hardship (R. 92-93) but states:

> In determining whether the Act requires that securities be registered, the honesty of the issuer, the soundness of the securities offered, or the delay and expense which may be involved in securing their registration, are not of material consequence.[24]

The Act indicates on its face that the Congress did give consideration to the relative burden of registration of small issues. Insofar as that consideration was made a basis for exemption, it originally set a limit of $100,000 and within that limit left the matter to the discretion of the Commission in the exercise of its rule-making authority. Section 3(b), as originally enacted, gave the Commission discretionary authority to exempt by rule, "subject to such terms and conditions as may be prescribed therein . . . if it finds that the enforcement of this title with respect to such securities is not necessary in the public interest and for the protection of investors by reason of the

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[24] Respondent's witness testified that the Company had already had occasion to prepare one registration statement in connection with an offering of preferred stock (R. 64-65). For that reason and because of the recurrent offerings of the common, compliance with the registration requirements of the Act would appear to be less burdensome for the respondent in proportion to the amount of money involved than would be the case where less frequent offerings might be involved.

small amount involved or the limited character of the public offering." The original $100,000 limit was in 1945 enlarged to the present $300,000. That exemption is inapplicable to the instant issue both because respondent's offering amounts to $800,000 and because respondent did not purport to comply with the conditions to exemption prescribed in the Commission's rules.[25]

It appears to have been the original expectation that the Commission would be sparing in the exercise of its discretionary authority to exempt under Section 3(b). Thus the Committee on Interstate and Foreign Commerce stated:

> To confer such a power upon the Commission permits the Commission by adequate rules and regulations to provide against needless registration of issues of such an insignificant character as not to call for regulation. This general power of the Commission, however, is closely limited by the requirement that it shall not extend to any issue whose aggregate amount exceeds $100,000. The Commission is thus safeguarded against any untoward pres-

[25] The Commission's rules pursuant to this section require filing of certain limited information with the Commission, including copies of any sales literature to be used, thereby serving to aid in the enforcement of the anti-fraud provisions of Section 17 applicable to such exempt issues. In addition, the Commission has prescribed certain minimum prospectus requirements applicable to certain types of issues. See Loss, *Securities Regulation* (1951) 379-390, for a description of the Commission's administration of this exemption. The Commission has recently made similar requirements as to a minimum prospectus more widely applicable. Securities Act Releases 3466; 3467; 18 Fed. Reg. 1437 (March 13, 1953).

sure to exempt issues whose distribution may carry all the unfortunate consequences that the act is designed to prevent." [H. Rep. No. 85, 73rd Cong., 1st Sess., (1933) p. 15.]

When Congress subsequently concluded to raise the limits of the Commission's discretion to a less "insignificant" amount, this change was made in recognition of the discretionary power of the Commission to deny or condition the exemption, and in the light of prior Commission rules providing a modicum of scrutiny with respect to the exempt issues.

e. In relying upon motive and lack of sales pressure the court below applied irrelevant critera.

The holding below emphasizes factors so irrelevant to the purposes of the Act as to make difficult any prediction as to its future application. The court below appeared to deem relevant the motive of the Company, which it found was to build up employer-employee relations rather than to raise capital. Nowhere in the terms of the Act nor in its legislative history, however, is there any indication that Congress intended the motives of the seller of securities to govern whether or not registration is necessary. To recognize the issuer's motives as a basis for exemption would be to widen the exemption so that it might be applicable to offerings not only to employees but perhaps also to stockholders, to customers, or even to groups

on the basis of ties of nationality.[26] As we have seen, the issuer's motives in dealing with any such group may be partly to afford a special opportunity to the group.[27]

Even if the Company's motive was not primarily to raise money, substantial sums were in fact raised by its sales to employees, sums so large that the Company would have been unable in several of the past years to have taken advantage of the Regulation A exemption for small offerings be-

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[26] Cf. *Securities and Exchange Commission* v. *Chinese Consol. Benev. Assn*, 120 F. 2d 738 (C.A. 2), where the group selling securities of the Chinese government apparently acted only from patriotic motives. *Cf.* also Section 6(c)(1) of the Public Utility Holding Company Act of 1935 [49 Stat. 803, 15 U.S.C. 79f(c)(1)], which prohibits the sale by any registered holding company or subsidiary thereof of securities of such holding company from "house to house," putting an end to the formerly prevalent "customer-ownership campaigns." It has been stated that the objective of these campaigns was not so much to raise capital as to stifle criticism that might be made by customers if they did not have a stake in the enterprise. Barnes, *Economics of Public Utility Regulation* (1942) 712; Utility Corporations, No. 72a (1935) 348-349, S. Doc. 92, 70th Cong. 1st Sess.

[27] In opposing the grant of a writ, respondent emphasized the relationship between its offering of stock to employees and its program of cash bonuses (Br. p. 3). The opinion of the district court states that recipients of bonuses have generally made investments in stock (R. 46). The Court of Appeals suggests that there was a substantial overlap between recipients of bonuses and the offerees (R. 91). As urged at pages 22-23, *supra*, under a proper interpretation of the term "offering" there was no factual basis for this conclusion. In any event, there is no more indication that the Congress intended to exclude recipients of bonuses from the protection of the Act than to exclude those employees whose compensation may be more regularly defined. Thus the relationship of the offering to the company's bonus program tends only to give color to the finding that the company's motive was not primarily to raise capital which, as indicated in the text, is a wholly irrelevant consideration.

cause its offering substantially exceeded the $300,000 statutory limitation. (See *supra*, pp. 33-35.)

The court below also appeared to rely on an absence of solicitation (R. 96). By this, the court apparently meant that employees were not *urged* to buy, since the record makes it clear that they were notified of the opportunity to buy (see pp. 4-5, *supra*). If the absence of high pressure sales techniques, however, should be considered significant in determining the extent of the non-public-offering exemption, a dangerous precedent would be created, since one of the oldest devices in marketing securities has been to make them seem hard to buy, to let the purchasers in on an "inside deal," or to make it seem that they, rather than the seller, are taking the initiative. Section 2(3) of the Act recognizes this situation by making a "solicitation of an offer to buy" the equivalent of an offer to sell.

The court below recognized that "the honesty of the issuer, the soundness of the securities offered, or the delay and expense which might be involved in securing . . . registration, are not of material consequence" (R. 93). By taking into consideration, however, such matters as the motives of the issuer and the lack of high-pressure selling, which we have seen have no necessary relationship to the statutory purpose, the court below fell into the error of making policy determinations in an area which, we submit, Congress did not leave open to the courts. We have seen that Congress carefully and in detail set forth the available exemptions and where it chose to delegate policy deter-

minations, they were delegated to this Commission within the carefully circumscribed limits of Section 3 (b) of the Act.

In *Securities and Exchange Commission* v. *W. J. Howey Co*, 328 U.S. 293, this Court refused to permit a similar consideration unrelated to the statutory purpose to be determinative of the scope of the registartion requirements of the Act, pointing out (p. 301): "The statutory policy of affording broad protection to investors is not to be thwarted by unrealistic and irrelevant formulae."

f. *The Commission's administrative construction rejected by the courts below is entitled to special weight.*

In the opinion of its General Counsel interpreting this exemption, which was released by the Commision at the outset of its administration of the Securities Act and has been forwarded ever since to persons inquiring as to the scope of the non-public-offering exemption, it was stated that the exemption was meant to apply only to offerings to "an insubstantial number of persons."[28] That opinion was given in the context of an offering to 25 persons and declined to express a definite con-

[28] Securities Act Release No. 285 (Jan. 24, 1935); 17 CFR Part 231, set forth at 11 Fed. Reg. 10952 (1946) and reprinted in full in the opinion below (R. 96-100). The portions of the release dealing with such matters as the number of units offered, the size of the offering, and the manner of offering (R. 98-100), relate to situations, not applicable here, where there are indications that the securities have been purchased for redistribution and hence a public offering may be involved even though the initial offering is to an insubstantial number of offerees.

clusion as to the availability of exemption. It made clear that there is no magic number which would mark the boundary of a private offering in every situation. With specific regard to employees, the release pointed out:

> . . . an offering to the members of a class who should have special knowledge of the issuer is less likely to be a public offering than is an offering to the members of a class of the same size who do not have this advantage. This factor would be particularly important in offerings to employees, where a class of high executive officers would have a special relationship to the issuer which subordinate employees would not enjoy.

But it was made clear that "an offering restricted to a particular group or class may, nevertheless, be a public offering if it is open to a sufficient number of persons."

The Commission's day-to-day administration of the exemption is reflected in hundreds of informal advisory interpretations of its staff dealing with varying types of proposed offers. The Commission has rarely acquiesced in an offering to more than one hundred persons. An example occurred in March 1951, when a corporation with over 100,000 employees requested a Commission interpretation whether or not an executive stock option program in which the number of participating employees would range from 100 to 220, depending upon the salary level chosen, would constitute a private offering. The Commission replied that it would

not insist upon registration if the company amended the plan to limit the offering to not more than 125 key executives, all of whom were fully familiar with the business affairs of the company.

We believe that the Commission's construction is significant, not only because it is the interpretation of the agency administering the Act[29] but also because there has been no proposal in Congress to amend the exemptive provisions here in-

[29] The weight to be accorded such an interpretation is suggested in *Securities and Exchange Commission* v. *Associated Gas & Electric Co.*, 99 F. 2d 795, 798 (C.A. 2): "Moreover, we are dealing with a new act the administration of which is the peculiar function of the Securities and Exchange Commission. One of the principal reasons for the creation of such a bureau is to secure the benefit of special knowledge acquired through continuous experience in a difficult and complicated field. Its interpretation of the act should control unless plainly erroneous. In no other way can the objects of the act be attained without constant and disconcerting friction." See *National Labor Relations Board* v. *Denver Building Council*, 341 U. S. 675, 690-692; *Boutell* v. *Walling*, 327 U. S. 463, 470-471.

The Commission's construction is consistent with the construction in a public release of the Federal Trade Commission (which agency administered the Securities Act of 1933 from the time of the enactment of that statute until the creation of the Securities and Exchange Commission in 1934). In its Securities Act of 1933 Release No. 97, at page 4, 17 CFR Part 231, set forth at 11 Fed. Reg. 10949 (1946), the Federal Trade Commission quoted a letter it had earlier written interpreting Section 4(1) of the Act, which stated:

> It is difficult to regard the contemplated offering of stock to 2,450 employees of the X corporation as not being a "public offering" within the meaning of Section 4(1) of the Securities Act. It is clear that the word "public" as used in this provision is not limited to offers which are made indiscriminately and open to anyone. For example, an offering confined to the security holders of a corporation may nevertheless be a "public offering" within the meaning of Section 4(1). Otherwise the first clause of Section 4(1) would be superfluous. Where a substantial number of persons is involved, it would seem imprudent to rely upon the second clause of Section 4(1) to give an exemption.

volved subsequent to the rejection by Congress of the 1934 proposal to exempt securities offered to employees.[30] Where Congress did see fit to increase the area of exemption, as we have seen, it did so by amending Section 3(b) of the Act to empower the Commission in its discretion to increase the conditional exemptions authorized by its rules from $100,000 to $300,000.

CONCLUSION

The order of the Court below should be reversed.

Respectfully submitted,

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APRIL 1953.

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[30] This Court has given "great weight" to acquiescence by Congress in a consistent administrative construction. *Costanzo* v. *Tillinghast*, 287 U. S. 341, 345; *United States* v. *Jackson*, 280 U. S. 183, 196-197.

APPENDIX

Section 2 of the Securities Act provides in pertinent part:

When used in this title, unless the context otherwise requires—

* * * * *

(3) The term "sale", "sell", "offer to sell", or "offer for sale" shall include every contract of sale or disposition of, attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value; except that such terms shall not include preliminary negotiations or agreements between an issuer and any underwriter.

* * * * *

Section 3(a) of the Act provides in pertinent part:

Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:

* * * * *

(9) Any security exchanged by the issuer with its existing security holders exclusively where no commission or other remuneration is paid or given directly or indirectly for soliciting such exchange;

(10) Any security which is issued in exchange for one or more bona fide outstanding securities, claims or property interests, or partly in such exchange and partly for cash, where the terms and conditions of such issuance and exchange are approved, after a hearing upon the fairness of such terms and conditions at which all persons to whom it is proposed to issue securities in such exchange shall have the right to appear, by any court, or by

any official or agency of the United States, or by any State or Territorial banking or insurance commission or other governmental authority expressly authorized by law to grant such approval;

Section 3(b) of the Act provides:

(b) The Commission may from time to time by its rules and regulations, and subject to such terms and conditions as may be prescribed therein, add any class of securities to the securities exempted as provided in this section, if it finds that the enforcement of this title with respect to such securities is not necessary in the public interest and for the protection of investors by reason of the small amount involved or the limited character of the public offering; but no issue of securities shall be exempted under this subsection where the aggregate amount at which such issue is offered to the public exceeds $300,000.

Section 4 of the Act provides:

EXEMPTED TRANSACTIONS

SEC. 4. The provisions of section 5 shall not apply to any of the following transactions:

(1) Transactions by any person other than an issuer, underwriter, or dealer; transactions by an issuer not involving any public offering; or transactions by a dealer (including an underwriter no longer acting as an underwriter in respect of the security involved in such transaction), except transactions within one year after the first date upon which the security was bona fide offered to the public by the issuer or by or through an underwriter

(excluding in the computation of such year any time during which a stop order issued under section 8 is in effect as to the security), and except transactions as to securities constituting the whole or a part of an unsold allotment to or subscription by such dealer as a participant in the distribution of such securities by the issuer or by or through an underwriter.

(2) Brokers' transactions, executed upon customers' orders on any exchange or in the open or counter market, but not the solicitation of such orders.

Section 5 of the Act provides:

PROHIBITIONS RELATING TO INTERSTATE COMMERCE AND THE MAILS

SEC. 5. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

(b) It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or

transmit any prospectus relating to any security registered under this title, unless such prospectus meets the requirements of section 10; or

(2) to carry or to cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of section 10.

Section 17 of the Act provides in pertinent part:

FRAUDULENT INTERSTATE TRANSACTIONS

SEC. 17. (a) It shall be unlawful for any person in the sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

* * *

(c) The exemptions provided in section 3 shall not apply to the provisions of this section.

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